

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
ALMARG COMPANY)

For Appellant: Brenda Marie Bailey
Certified Public Accountant

For Respondent: James C. Stewart
Counsel

O P I N I O N

This appeal is made pursuant to section 26075, subdivision (a), of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Almarg Company for refund of franchise tax in the amount of \$2,520.00 for the year 1976.

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The issue for **determination** is **whether** a taxpayer on the accrual method of accounting may report on a deferred payment basis the gain from the sale of its inventory and other personal property.

Appellant is a California corporation. During 1976 appellant's primary activity consisted of retail sales and it used the accrual method of accounting. During that year appellant sold all of its inventory, furniture and fixtures, and accounts receivable less accounts payable. The basis of the assets sold was \$1136,150 and the selling price of the property was \$165,000. Appellant reported the sale on its tax return as follows:

Computation of Gain

Selling price	\$165,000
Easis of property	<u>(136,150)</u>
Gain to be realized	<u>\$28,850</u>

Gain to be Recognized

Cash	\$53,000
Mkt. value of note (75% of \$112,000)	84,000
	<u>\$137,000</u>
Less: Cost of property	<u>(136,150)</u>
Gain recognized in year of sale	<u><u>\$ 850</u></u>

Respondent determined that appellant, as an accrual basis taxpayer, was required to report the entire \$28,850 gain in 1976, the year of sale. Respondent therefore issued a proposed assessment based on that determination. Appellant filed a protest, but after due consideration, respondent affirmed its assessment. Appellant then paid the additional tax and filed a claim for refund. Respondent's denial of that claim led to the filing of this appeal.

Appellant's position is based primarily on the premise that it need only recognize in 1976 the fair market value of the buyer's note mentioned above. This position is said to be founded on Internal Revenue Service publication 537 (Installment and Deferred Payment Sales). For the reasons stated below, we conclude that appellant's reliance on that publication is misplaced.

Since appellant's sale involved future payments but the initial amounts paid exceeded 30 percent of the selling price, the installment method of reporting was not applicable. Appellant acknowledges this but argues that it may report the sale at issue under the other deferred payment method. Under this latter method, the buyer's obligations may be reported at their fair market value. however, it has been determined by the **courts** that an accrual basis taxpayer making **a** casual sale of personal property does not qualify to report the results of the sale on the other deferred payment method. (See, e.g.,

George L. Castner Co., 30 T.C. 1061 (1958); Western Oaks Wilding Corp., 49 T.C. 365 (1968); Jones Lumber Co., Inc. v. Commissioner,

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¶ 67,081 P-H Memo. T.C. (1967), affd., 404 F.2d 764 (6th Cir. 1968); George E. Freitas, ¶ 66,105 P-H Memo. T.C. (1966); Baltimore Baseball Club, Inc. v. U.S., 32 Am. Fed. Tax R.2d 5352.) That particular method is available only for sales of realty by virtue of Treasury Regulation. § 1.453-6 and its predecessor regulations. Since that regulation is substantially similar to respondent's regulations on the same subject (see Cal. Admin. Code, tit. 18, reg. 24667-24673.5(f)), and since the respective state and federal statutes under which those regulations were promulgated are also substantially similar (see Internal Revenue Code section 453 and former Revenue and Taxation Code sections 24667 et. seq.), federal case law in this area is highly persuasive in interpreting the California provisions. (Rihn v. Franchise Tax Board, 131 Cal.App.2d 356, 360 [280 P.2d 893] (1955).) On the basis of the above-cited federal cases, we believe appellant is not entitled to report gain from the sale at issue on the other deferred payment method, but must instead include all future payments in income at the time of the sale, i.e., when the taxpayer acquires the right to receive those amounts in the future. (Western Oaks Building Corp., supra; First Savings & Loan Association, 20 T.C. 474 (9) (1953).) Moreover, when property is sold, it is the face amount of the right, not its fair market value, which must be treated as received and includable in income." - (Western Oaks Building Corp., supra, citing First Savings & Loan Association, supra.) Therefore, there is no basis for the fair market valuation procedure that appellant attempted to apply to the note it received as part of the sale proceeds. 1/

We also must mention that the example cited by appellant in Publication 537 concerned a sale of real property. Additionally, the three cases that appellant cited all concerned sales of realty by cash-basis taxpayers. All of these items are, of course, consistent with the principles discussed above.

For the foregoing reasons, we must conclude that respondent acted properly in requiring appellant, an accrual basis taxpayer, to report its entire \$28,850 gain in 1976, the year of sale. No deferred payment method was applicable.

1/ There is another rule applicable to accruals that neither party has addressed. Where the facts are such that the item in question is uncollectible when the obligation therefor accrues, and there is little or no likelihood of collection in the future, a taxpayer on the accrual basis is not required to report such income. (Corn Exchange Bank v. United States, 37 F.2d 34 (2d Cir. 1930); Joy Manufacturing Co., 23 T.C. 1082 (1955).) However, the record does not show that the note at issue was uncollectible.

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this **proceeding**, and good cause appearing **therefor**,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Almarg Company for refund of additional franchise tax in the amount of \$2,520 for the year 1976, be and the same is hereby sustained.

Done at Sacramento, California this 15th day of September, 1983, by the State Board of Equalization, **with** Board Metiers Mr. Bennett, Mr. Collis, Mr. Dronenburg, Mr. **Nevins** and Mr. Harvey present.

<u>William M. Bennett</u>	, Chairman
<u>Conway H. Collis</u>	, Member
<u>Ernest J. Dronenburg, Jr.</u>	, Member
<u>Richard Nevins</u>	, Member
<u>Walter Harvey*</u>	, Member

*For Kenneth Cory, per Government Code section 7.9